86-725 (1)

No. ______

IN THE

Supreme Court of the United States

OCTOBER TERM, 1986

ROY E. DOOLEY, JR., et al.,

Petitioners,

v.

AMERICAN AIRLINES, INC., et al.,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

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QUESTIONS PRESENTED

A. Section 204(g) of the Employee Retirement Income Security Act ("ERISA") prohibits an employer from amending a pension plan in a manner which decreases a participant's accrued benefits. Section 402(b)(4) of ERISA requires each plan to be maintained pursuant to a written instrument which, among other things, specifies the basis on which benefit payments are to be made. American Airlines changed the discount rate used to calculate the lump-sum optional form of the normal retirement benefit under its pilots' retirement plan from 8½% to a floating rate which, in 1981 and 1982, was significantly higher than 8½%, with the result that pilots retiring during that period received substantially reduced lump-sum payments. The Seventh Circuit Court of Appeals found that American did not violate Section 204(g) of ERISA because the plan expressly authorized American to set the discount rate and the change in the rate resulting from American's exercise of that discretion did not constitute a plan "amendment".

The questions presented are:

(1) Whether a plan provision which permits an employer, in its discretion, to determine one or more of the bases on which benefit payments are to be made, satisfies the requirements of Section 204(g) of ERISA and the broad remedial purposes of ERISA.

(2) Whether the Seventh Circuit's restrictive reading of ERISA Section 204(g)'s prohibition of plan amendments having the effect of reducing accrued benefits, in which the court either excludes from the term "amendment" discretionary employer changes in the actuarial assumptions used to calculate the lump-sum optional form of benefit, or else treats those assumptions as not part of the "plan" for purposes of that Section, is consistent with the language and broad remedial purposes of ERISA.

(3) Assuming that Section 402(b)(4) of ERISA requires specification in the Plan document of the basis of benefit payments in a manner which precludes employer discretion, or that the actuarial assumptions used for purposes of determining the equivalence of optional forms of benefit are part of the "plan" and changes in those assumptions therefore constitute "plan amendments" under Section 204(g), did American's change in assumptions result in decreases in petitioner's accrued benefits?

B. The IRS in 1979 gave existing pension plans like American's until 1984 to comply with the Internal Revenue Code requirement that actuarial assumptions, such as the discount rate at issue in this case, be included in the formal Plan document. Such action served to preserve American's tax deduction. The question presented is:

Whether the IRS has the authority to relieve American of its pre-existing substantive fiduciary duties to petitioners and other Plan participants under Title I of ERISA by postponing the date on which American must comply with corresponding tax code provisions when such authority, to the extent that it is granted at all, is delegated solely to the Secretary of Labor.

LIST OF PARTIES

The parties to the proceedings below were the Petitioners Roy E. Dooley, Jr., Thomas F. Latta, Lionel T. Alexander, Lowell W. Armstrong, Buford O. Baker, W.S. Baugh, Alvin O. Berg, Jr., E. G. Bielinski, John W. Blute, Vincent R. Bradley, William H. Burgess, Hugh T. Clark, Byron S. Cramblet, Frank J. Cusare, Clarence O. Day, Jr., E.R. Dozier, Clyde E. Driggers, R. M. Euwema, J. R. Fitzgerald, William D. Fulton, Ralph E. Green, Walter J. Gromel, William J. Goeke, Frank G. Hart, F. J. Hazzard, Howard F. Jenkins, Jr., James G. Johnson, Frank Kaplowitz, Norman L. Kleman, W.C. Kraemer, A. P. Lang, H. D. Leavell, Ralph W. Long, Jr., Dale F. Mabry, Joseph K. Marks, Robert W. Martin, Boniface J. Mayer, Edward O. McKown, Jr., Harold R. Miller, H. C. Milton, George A. Moculski, Earl M. Morrow, Stanley R. Nielsen, Arne E. Oas, George A. Oden, Wayne C. Parris, Robert K. Parsons, Angelo B. Perriello, J. C. Pollard, Edward C. Price, Russell A. Quandt, John J. Ranck, Harvey R. Rice, H. E. Rogers, W. J. Roth, J. M. Rutledge, R. C. Speck, and Willard I. Staples, and the respondents American Airlines, Inc., the American Airlines, Inc., Fixed Income Plan of the Pilot Retirement Benefit Program, G. E. Overbeck, T. G. Plaskett, T. F. Quinn, Jr., C. A. Pasciuto and N. W. Byl. The above named petitioners and respondents include all of the parties to the proceedings below and in this Court.

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Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

Petitioners respectfully pray that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Seventh Circuit, entered in the above proceeding on August 5, 1986.

OPINIONS BELOW

The opinion of the United States Court of Appeals for the Seventh Circuit is reported at 797 F.2d 1447; it is reprinted in Appendix A hereto, p. A-1, *infra.* The memorandum opinion and order of the United States District Court for the Northern District of Illinois, Eastern Division (Parsons, J.) is unreported; it is reprinted in Appendix A hereto, p. A-15, *infra.*

JURISDICTION

Petitioners brought this action in the United States District Court for the Northern District of Illinois, invoking federal jurisdiction under 28 U.S.C. §§ 1331 and 1337(a) and 29 U.S.C. § 1132(e). On April 17, 1985, the district court

denied petitioners' motion for summary judgment on Count I of their third Amended Complaint and granted respondents' motion for summary judgment on Counts I to IV inclusive. *See* p. A-15, *infra*.

On August 5, 1986, the Seventh Circuit affirmed the district court with respect to Count I and reversed with respect to Counts II-IV. *See* p. A-1, *infra*. Petitioners did not seek rehearing.

The jurisdiction of this Court to review the judgment below rests on 28 U.S.C. § 1254(1).

STATUTES AND REGULATIONS INVOLVED

This action involves the application and interpretation of the following Sections of the Employee Retirement Income Security Act (ERISA): 3(1), (2), and (3); 204(g); 402(a); 402(b)(4); 414 and 502(a). 29 U.S.C. §§ 1002(1), (2), and (3); 1054(g); 1102(a); 1102(b)(4); 1114 and 1132(a). Sections 411(d)(6) and 7805(b) of the Internal Revenue Code are involved, 26 U.S.C. §§ 411(d)(6) and 7805(b), as well as Section 1.401-1(b)(1)(i) of the Income Tax Regulations. Each of these authorities is reprinted in Appendix B, B-1, *infra*.

STATEMENT OF THE CASE

Nature of the Case

Petitioners are fifty-eight airline pilots who retired from service with American Airlines, Inc. at various dates between February 1, 1981 and October 1, 1982. (Dk. No. 67, ¶¶ 2(a)-(eee); Dk. No. 81, ¶¶ 2(a)-(eee.)[1]

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[1] For purposes of this petition, the reference "Dk. No." refers to the Docket Number of the cited document in the Record on Appeal, as transmitted from the district court.

Respondents, sued in their capacities as ERISA fiduciaries, are American Airlines, Inc., the American Airlines, Inc. Fixed Income Plan of the Pilot Retirement Income Program (the "Plan"), and five individual members of American's Pension Benefits Administration Committee (referred to, collectively, as "American"). Petitioners seek to recover benefits due them and to enforce their rights under the Plan, pursuant to Section 502(a) ERISA, 29 U.S.C. § 1132(a).[2]

The Pleadings

The dispute arises from American's change in the interest rate used to calculate the lump-sum optional form of retirement benefit under the Plan. Effective February 1, 1981, American changed the discount rate used to calculate the present (lump-sum) value of a participant's normal retirement annuity from a fixed rate of 8½% to a variable rate of 1% greater than the prevailing interest for corporate bonds rated Aaa by Moody's Investor Services, a change which, during the relevant time period, virtually doubled the interest rate used. As a result, when petitioners retired and elected the lump-sum optional benefit, they received on an average appoximately 30% less than they would have received had their lump sums been computed using an 8½% assumption. The economic savings realized by the Plan as a result of reduced payments to petitioners (and other participants electing lump-sum benefits in 1981 and 1982) is passed through to American, by operation of the actuarial cost method used by the Plan, in the form of reduced future contributions over a fifteen-year period.

Count I of the Third Amended Complaint (Dk. No. 67) alleged that, as implemented by American,[3] the change in

[2] Section 502(a) as well as the other stutotes and regulations relevant to petitioners' claims are reproduced in Appendix B.

[3] Petitioners do not contend that American may not alter or increase the interest assumption. Petitioners contend only that, in making such changes, American may not reduce the amount

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interest assumption constituted a Plan amendment resulting in an impermissible reduction in petitioners' accrued benefits in violation of Section 204(g) of ERISA, 29 U.S.C. § 1054(g).[4] In their Answer (Dk. No. 81), respondents contended that the change in interest assumption "had the purpose of maintaining the actuarial equivalence of lump-sum distributions to the Plan members" (*Id.* ¶ 10, p. 35), and denied that adoption of the change was improper.

Proceedings and Disposition in the Courts Below

Petitioners moved for partial summary judgment as to liability on Count I of their Third Amended Complaint on the ground that, as a matter of law, the change in the interest assumption constituted a violation of Section 204(g) of ERISA. (Dk. Nos. 69-70, 104-06.) Respondents filed a cross-motion for summary judgment on the ground that the change in interest assumption constituted administrative action permitted by the Plan. They also sought summary judgment as to Counts II, III and IV on various grounds. (Dk. Nos. 83-85, 113-14, 118.)

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of participants' lump-sum entitlements based on their service up to the date of the change. *See Rev. Rul.* 81-12, 1981-1 C.B. 228 (describing methods for changing interest assumptions without reducing accrued benefits).

[4] Count II alleged that the variable interest rate adopted by American was unreasonably high during the relevant period and resulted in lump-sum benefits which were less than actuarially equivalent to the annuities to which petitioners were entitled, in violation of the vesting provisions of Section 203 of ERISA, 29 U.S.C. § 1053. Count III alleged that the change in interest assumption was motivated by respondents' desire to secure for American the economic benefit of the reduced lump-sum payments, in violation of Section 404(a)(1)(A) of ERISA, 29 U.S.C. § 1104(a)(1)(A), which requires respondents as Plan fiduciaries to discharge their duties solely in the interest of the participants and beneficiaries. Count IV sought injunctive relief against the wrongful conduct asserted in Counts I through III.

The district court, on April 17, 1985, pursuant to a Memorandum Opinion and Order which refers only to the issues as to Count I, denied the Pilots' motion for partial summary judgment and granted American's motion for summary judgment as to all Counts of the Third Amended Complaint. (Dk. No. 119.)

On appeal, the Seventh Circuit affirmed the district court's judgment as to Count I and reversed as to Counts II through IV. No party sought rehearing.

The American Fixed Income Plan of the Pilot Retirement Benefit Program

The American Airlines Plan is a "defined benefit pension plan" which provides that, upon retirement at age 60, a pilot is entitled to receive a Basic Retirement Annuity consisting of a monthly pension equal to 1.25% of his final average compensation multiplied by a number equal to one less than the number of years of his credited service. (Dk. No. 67, ¶¶ 3(b), 5, 7, Exhibit A; Dk. No. 81, ¶¶ 3(b), 5, 7.)

Under Section 10.2 of the Plan, the normal benefit is a qualified joint and survivor annuity in the case of married participants and a single life annuity in the case of unmarried participants. (Dk. No. 67, Ex.A, § 10.2, pp. A37-38.) Section 10.4 of the Plan gives a participant the right to elect his benefit in one of a number of optional forms. (Dk. No. 67, Exhibit A, ¶ 10.4, pp. A39-41.)

Adoption of the Lump-Sum Optional Form of Benefit Discounted at 8½%

Prior to October 1978 the Plan did not provide for a lump-sum form of benefit. (Dk. No. 67, ¶ 7; Dk. No. 81, ¶ 7.) Section 10.4(c) of the Plan provided:

> (c) *Open Option.* A member may elect, if the Administrator consents thereto on a basis of policies uniformly applicable to all Members similarly situated, to receive his or her Basic Retirement Annuity . . . in an optional

> form other than one specifically provided in this Section . . .

Section 10.4 also provided that "[a]ny optional form of Basic Retirement Annuity elected pursuant to this Section shall be the Actuarial Equivalent of an annuity payable for the lifetime of the member only in an annual amount equal to such Basic Retirement annuity. . . ." Article II, § (d) of the plan document defines "actuarial equivalent" as "the equivalent in value on the basis of actuarial factors *approved from time to time by American Airlines. . . .*" Article II, § (d) (emphasis added).

On October 26, 1978, American issued Employee Bulletin No. 547-78 announcing the adoption of a lump-sum optional benefit. The Bulletin stated in part:

> The Company and the Allied Pilots Association have agreed to allow lump sum distributions at retirement from the Pilot Retirement Benefit Plan. This form of payment would be granted under the Open Option and is offered in addition to the various forms of payment provided under the Plan.
>
> Distributions will be based on the annual benefit otherwise provided under the Plan multiplied by a lump-sum annuity factor. The factor is developed using an 8½% interest rate and the 1971 Group Annuity Mortality Table. . . . (Dk. No. 67, Exhibit B.)

Thus the lump-sum option, at its inception, involved an 8½% fixed actuarial assumption which was used to discount to present value the total payments a pilot would otherwise have received under his Basic Retirement Annuity.

The Change in the Interest Assumption

In December 1979, by Employee Bulletin No. 497-79[5], American announced that, for pilots retiring after January

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[5]Though dated December 26, 1979, the Bulletin did not actually reach the employees until January 3, 1980. (Deposition of

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1, 1981, the interest assumption used to calculate lump-sum distributions under the Plan would be changed:

> Effective for retirements after January 1, 1981, the interest rate used in calculating lump sum distributions from the American Airlines Retirement Benefit Plans will be a rate one percentage point higher than the Moody's Aaa Corporate Bond Rate for the second month preceding the retirement date. Thus, if a participant retires June 1, the rate used in calculating a lump sum distribution will be the Moody's Aaa Corporation Bond Rate for April, plus one percentage point. . . . (Dk. No. 67, ¶ 8, Exhibit C; Dk. No. 81, ¶ 8.)

On April 22, 1980, in Employee Bulletin No. 161-80, American modified the variable interest assumption. (Dk. No. 67, ¶ 9, Exhibit D; Dk. No. 81, ¶ 9.) The Moody's Aaa Corporate Bond Rate used was changed to the rate for the third month prior to retirement; and the "Moody's plus one" rate was phased in at 2% per month over a period of several months beginning with a rate of 10½% as of February 1981. (*Id.*)[6]

The Effect of the Changed Assumption on Lump-Sum Distributions

The yields on Moody's Aaa long-term corporate bonds rose steadily from 8.89% in October 1978, when the lump-sum option based on the 8½% assumption was first adopted, to 10.74% in December 1979. (Dk. No. 85, Exhibit C, at Exhibit

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T. F. Quinn, January 13, 1983, p. 34.) The delay in distribution, coupled with the requirement of election of the lump sum at least one year prior to retirement, meant that the earliest date on which a pilot could retire after learning of the change in assumption was February 1, 1981, too late to avoid the impact of the changed assumption.

[6] The "phase-in formula" in fact overtook the "Moody's plus one" rate in May, 1981 (Dk. No. 85, Ex. C). Thus the new interest assumption was fully effective for participants retiring on and after May 1, 1981.

II thereto.) Between February 1981 and October 1982, when petitioners were retiring, the Moody's rate ranged from a low of 12.12% to a high of 15.49% and thus produced lump-sum discount rates peaking at 16.49% for participants who retired on December 1, 1981. (*Id.*)

As a result, petitioners and other participants retiring in 1981 and 1982 who elected lump-sum payments received significantly smaller amounts under the new variable interest assumption than they would have received under the 8½% rate. (Dk. No. 69, Exhibit A.)

The Relationship Between the Interest Assumption and Plan Financing

The Plan is financed exclusively by contributions of American as the sponsoring employer. (Dk. No. 67, Exhibit A, § 51, pp. A13-14.) Each year, American makes a contribution to the Plan in an amount, determined by the Plan actuary in accordance with the actuarial cost method used by the Plan,[7] which, together with past and future contributions and investment earnings on all contributions, will be sufficient to pay the expenses of administering the Plan and to accumulate sufficient funds over the working lives of the participating employees to pay them their promised pension benefit when they reach retirement age. In computing the employer's annual contribution, the Plan actuary therefore must take into account, among other things, anticipated investment earnings and the amount of the contribution thus depends, in part, upon the rate of investment return the actuary assumes the Plan will realize. The actuarial assumption—the interest assumption for funding purposes—was 8½% prior to 1981; when the 1981 actuarial valuation was made in May of 1982, the interest assumption for funding purposes for active employees was increased to 9½%.

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[7] The manner of computing American's annual contribution is described in detail in the Affidavit of Carl H. Fischer, petitioners' expert. (Dk. No. 106.)

The interest and other actuarial assumptions utilized by the actuary in computing the employer's contributions represent only the actuary's best estimate of future experience. (Dk. No. 106, pp. 17-18.) In practice, the Plan's actual experience may—and usually will—vary to a greater or lesser extent. (*Id.*) When the Plan's actual investment experience in any plan year is more favorable than the actuarial assumption, an "actuarial experience gain" occurs, measured by the difference between the actual rate of return experienced by the Plan and the rate of return the actuary assumed. (*Id.*) This gain is amortized and applied by the actuary in computing contributions for future plan years. (*Id.*) When Plan assets earn more than the interest assumption for funding purposes, thereby producing an actuarial experience gain, the employer's contributions will be less, all other things being equal, than would otherwise be the case; the amount of the excess earnings are effectively passed through to the employer and ultimately completely appropriated by it, in the form of savings on future contributions. (*Id.*) The pass through would be accomplished in approximately 11.4 years under the actuarial cost method being used by American in 1981, and in 15 years under the cost method adopted in 1982. (*Id.*, pp. 18-19, 21, 22.)

The effect of paying a lump-sum distribution computed on the basis of an interest assumption in excess of the interest assumption used for funding purposes—as was the case with the lump-sum distributions to petitioners under the variable interest assumption—is exactly the same as an actuarial gain from investment experience, and the economic benefit of that gain is passed through to American in precisely the same way, over a period of 15 years under American's current actuarial cost method (*Id.*, pp. 24-26).[8]

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[8] Both Kenneth E. Polk, the consulting actuary serving as Plan actuary at the time of the change in interest assumption, and Willard A. Hartman, respondents' actuarial expert, agree that the effect of paying lump sum distributions discounted at rates in excess of the interest rate used for funding purposes is

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REASONS FOR GRANTING THE WRIT

I.

The Seventh Circuit Decided Important Questions of Federal Law Which Must Be Settled In Order to Insure the Enforceability of Basic Rights Under ERISA

Count I of the complaint alleged that American's change in actuarial assumptions used to calculate the present value of the lump-sum retirement benefit from an 8½% to a floating rate constitutes a reduction in participants' accrued benefits by an amendment to the plan, in violation of Section 204(g) of ERISA, 29 U.S.C. § 1054(g). Section 204(g) provides, with exceptions not relevant here, that a participant's accrued benefit[9] under a plan may not be decreased by a plan amendment.

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the same as an experience gain on investments and that that gain is passed through to American in the form of reduced future contributions (Deposition of Ken E. Polk, January 12, 1983, pp. 137-14; Dk. No. 117, Exhibit X, 43-47).

[9] The Pilots' "accrued benefits" include the lump-sum optional form of their normal retirement benefit. Treasury Regulation § 1.411(a)-7(a)(1) explicitly states that "[t]he accrued benefit includes any optional settlement at normal retirement age", and Treasury Regulation 1.411(d)-(3)(b) makes clear that plan amendments altering actuarial assumptions violate Section 411(d)(6) of the Internal Revenue Code (the Code analog to ERISA Section 204(g)) if they result in reduction of participants' accrued benefits so defined. These regulations are authoritative with respect to interpretation of Section 204 of ERISA (*see*, ERISA § 3002(c), 29 U.S.C. § 1202(c)) and, being legislative in character and not obviously repugnant to the statutory purpose, are binding on the courts. *Batterton v. Francis*, 432 U.S. 416, 425-26 (1977); *Baker v. Otis Elevator Co.*, 609 F.2d 686 (3d Cir. 1979); *Anderson Bros. Ford v. Valencia*, 452 U.S. 205, 219 (1981). In similar circumstances, the Second Circuit has held that early retirement benefits are part of the accrued benefit. *Amato v. Western Union International, Inc.*, 773 F.2d

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The court of appeals held that there was no violation of Section 204(g) because the plan expressly authorized American to establish and alter the actuarial assumptions used to determine the equivalence of optional forms of benefit and,

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1402 (2d Cir. 1985) *cert. dismissed* 106 S. Ct. 1167 (1986); *but, cf. Bencivenga v. Western Pennsylvania Teamsters & Employers Pension Fund,* 763 F.2d 574 (3d Cir. 1985). Moreover, in the Retirement Equity Act of 1984 ("REA"), Pub. L. 98-397, Congress clarified the law to eliminate any doubt that optional forms of the normal retirement benefit are part of the accrued benefit protected from reduction by ERISA Section 204(g). Section 301(a)(2) of the REA amended Section 204(g) of ERISA to provide expressly that, for purposes of the prohibition against reductions in accrued benefits, "a plan amendment which has the effect of . . . eliminating an optional form of benefit, with respect to benefits accrued before the amendment, shall be treated as reducing accrued benefits". Thus, there can be no doubt subsequent to REA that a plan participant's "accrued benefit" for purposes of Section 204(g) includes optional forms. The Senate Finance Committee Report on REA is at pains to state that the modification to Section 204(g) of ERISA merely "clarifies" the scope of the prohibition and that "[t]he committee intends that no inference is to be made on the basis of this clarification as to the scope of the prohibition before the effective date of the provision". Senate Report No. 575, 98th Cong., 2d Sess., pp. 27-28, *reprinted in* [1984] *U.S. Code Cong. & Adm. News*, pp. 2573-74. Under familiar canons of statutory construction, the statement in the Committee Report negating inferences must be taken as buttressing the Congressional intention to clarify existing law rather than to change it. Under those circumstances, the language of the clarifying statute "is persuasive authority of the proper construction of the original [act]". *Brown v. Marquette Savings and Loan Ass'n*, 686 F.2d 608, 614-15 (7th Cir. 1982).

Petitioner's argument is that the increase in the interest assumption resulted in a reduced payment with respect to the portion of a participant's benefit earned *before* the change in assumption. As such it is an impermissible reduction in the accrued benefits of affected participants.

therefore, the change did not constitute a plan amendment. In so holding the court stated that it did not reach the question "whether the actuarial assumptions—contained, as they were, in bulletins which were physically distinct from the pension plan document—can be construed as part of the pension plan for purposes of ERISA."

Underlying the court of appeals' decision are two premises, both of which raise important questions as to the proper interpretation of ERISA. The first premise, more or less expressly stated by the court, is that the requirement of ERISA Section 402(b)(4) that every plan must specify the basis of benefit payments can be satisfied by a provision which permits the employer to determine the basis of such payments in its discretion. The court expressly rejected petitioners' argument that the purpose of that section, properly construed in the larger context of the statutory objectives of ERISA, is to make the rights and entitlements of plan participants objectively determinable and to preclude the intervention of employer discretion—a purpose directly analogous to the requirement under Treasury Regulation 1.401-1(b)(1)(i) that a pension plan must provide "definitely determinable benefits" in order to be a qualified plan under Section 401(a) of the Internal Revenue Code. The Internal Revenue Service has construed its "definitely determinable benefits" rule to mean that benefit levels may not be subject to employer discretion (*see*, Rev. Rul. 74-385, 1974-2 C.B. 130), and that the actuarial assumptions used to determine equivalence of optional forms of the normal retirement benefit must be set forth in the formal plan document (Rev. Rul. 79-90, 1979-1 C.B. 155).

The second, entirely unstated premise of the Seventh Circuit's decision is that the rules adopted by an employer pursuant to such a discretionary provision do not themselves become part of the "plan" for ERISA purposes so that when, by a later exercise of its discretion, the employer changes those rules there is no "amendment" to the "plan" which would call into play the safeguards of Section 204(g).

According to the court of appeals, it would "contort the plain meaning of 'amendment'" to apply that term to changes resulting from "the valid exercise of a provision which was already firmly ensconced in the pension document." Slip. Op. at 9, *infra* A-9. In short, the court below construed Section 204(g)'s proscription against reductions in accrued benefits "by an *amendment of the plan*" to reach only those reductions resulting from changes in the "pension document," adopted, presumably, in accordance with the formal amendment procedure provided in that document. Thus, notwithstanding the court's disclaimer, it necessarily decided that rules dehors the formal plan document, such as the actuarial assumptions here at issue, are not part of the "plan" for purposes of Section 204(g), even though those rules determine "the basis of payments . . . from the plan" and are therefore required by Section 402(b)(4) to be "specif[ied]" by the "plan."

The court of appeals' interpretation of the ERISA Section 402(b)(4) requirement that the plan must specify the basis on which payments are made as permitting employer discretion, and its implicit restrictive interpretation of the meaning of the term "plan" are at odds with the language and purpose of the statute, conflict with decisions of other circuits which have interpreted the term "plan" in ERISA, and, if allowed to stand, will seriously weaken protections ERISA was enacted to provide.

A. Whether a provision authorizing an employer, in its discretion, to establish and alter rules determining the amount of participants' benefit entitlements, satisfies the requirement of ERISA § 402(b)(4) that a plan must specify the basis for benefit payments.

As made clear in Section 2 of ERISA, 29 U.S.C. § 1001, ERISA was born of a Congressional determination that comprehensive legislative action was required in order to protect employees from loss of anticipated retirement benefits. Among the measures adopted by Congress for accomplishing that overriding purpose were extensive provisions designed

to insure full disclosure to plan participants of their rights and obligations under the plan, as well as substantive provisions designed to safeguard employee benefit entitlements from inequitable loss or reduction. Section 402(b)(4) is clearly designed to provide both forms of protection.

The Conference Committee, in its Report on the bill which was ultimately enacted, explained the purpose of Section 402:

> A written plan is to be required in order that every employee may, on examining the plan documents, determine exactly what his rights and obligations are under the plan . . .
>
> . . . [T]he plan documents are to set out the basis for contributions to and payments from the plan. Thus, the plan is to specify what part (if any) of contributions are to come from employees and what part from employers. Also, it is to specify the basis on which payments are to be made to participants and beneficiaries. (H. Conf. Rep. No. 93-1280, 93d Cong. 2d Sess. 297, *reprinted in* [1974] U.S. Code Cong. & Adm. News 5023, 5077.)

In addition to this clearly-intended disclosure function, it is also apparent that the requirement that the plan specify the basis of benefit payments, coupled with the provision of Section 404(a)(1)(D) of ERISA requiring plan fiduciaries to discharge their duties in accordance with "the documents and instruments governing the plan" and Section 204(g)'s prohibition of plan amendments which have the effect of reducing accrued benefits, also provides a significant substantive safeguard for plan participants. It is equally apparent that a plan provision which "specifies" that the basis of benefit payments is to be determined, in whole or in part, by the employer in its discretion defeats both the disclosure and the protective purposes of Section 402.

Moreover, the holding of the court below creates a distinction between pension plans qualified under Section 401(a) of the Internal Revenue Code and nonqualified plans on this

critical point. Here the court of appeals has said that Section 402(b)(4) of ERISA—which applies to all plans, qualified and nonqualified—is not offended by a provision permitting employer discretion. Such a provision, however, is clearly not permissible under Section 401(a) of the Code. For many years prior to enactment of ERISA, regulations under Section 401(a) had defined a qualified pension plan as a "definite written program and arrangement" which is "established and maintained by an employer primarily to provide systematically for the payment of definitely determinable benefits to his employees over a period of years, usually for life, after retirement." Treas. Reg. §§ 1.401-1(a)(2), 1.401-1(b)(1)(i); *Guides for Qualification of Pension, Profit Sharing and Stock Bonus Plans*, IRS Pub. 778, Part 2, ¶¶ (f), (m), *reprinted in* CCH Pen. Plan Guide ¶ 17,003. The purpose of the definitely determinable benefits requirement is to insure that the amount of benefits "is not subject to the discretion of the employer." Rev. Rul. 74-385, 1974-2 C.B. 130.

The effectiveness of these regulations has continued since enactment of ERISA (*see*, Treas. Regs. § 1.401(a)-1(b)) and the IRS has since had occasion to consider its "definitely determinable benefits" requirement in the context of actuarially equivalent optional forms of benefit:

> *Whenever the amount of a benefit in a defined benefit plan is to be determined by some procedure (such as "actuarial equivalent", "actuarial reserve", or "actuarial reduction") which requires the use of actuarial assumptions (interest, mortality, etc.) the assumptions to be used must be specified within the plan in a manner which precludes employer discretion.* For purposes of this revenue ruling, employer discretion includes discretion of the employer, plan administrator, fiduciary, actuary, etc. (Rev. Rul. 79-90, 1979-1 C.B. 155, 156.) (Emphasis added.)

Revenue ruling 79-90 goes on to state that plans may comply either by incorporating a fixed standard using specified assumptions or a table of adjustment factors, or by adopting a variable standard which indexes the assumption to some

objective, self-adjusting standard such as the prime rate of interest.[10] In Revenue Ruling 81-12, 1981-1 C.B. 228, the IRS further held that changes in actuarial assumptions may result in impermissible reductions in participants' accrued benefits and illustrated techniques for changing the assumptions while safeguarding benefits from being unlawfully reduced.

Thus, the IRS clearly interprets its "definitely determinable benefits" rules as necessitating the specification in the formal plan document of the actuarial assumptions used to determine equivalence of optional forms of benefit, in a manner which precludes employer discretion. That requirement, as a practical matter, will now have to be met by all defined benefit pension plans as a condition of qualification

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[10] Revenue Ruling 79-90 deferred its effectiveness for noncomplying plans in existence on the date of its issuance—such as the American plan—until plan years beginning on or after December 31, 1983. Because of this "grace period" for compliance, the court of appeals "[saw] no reason to immediately impose upon American a provision with which it was given years to comply." Slip Op. at 11, *infra* A-11. The court below did not separately analyze the meaning of Section 402(b)(4) of ERISA, or attempt to interpret that Section in light of its purpose or the overriding purposes of Title I of ERISA. Instead it focused upon a narrow and technical interpretation of the meaning of the term "amendment" without regard to the statutory objectives, placing entire reliance upon an inapposite case arising under Section 203(a)(3)(E) of ERISA, 29 U.S.C. § 1053(a)(3)(E), a specialized provision applicable only to multiemployer pension plans and not to single-employer plans like American's. See discussion of *Stewart v. National Shopmen's Pension Fund*, 730 F.2d 1552 (D.C. Cir. 1984), at pp. 25-27, *infra*. The effect of the court of appeals' decision is to postpone the effectiveness of the substantive provisions embodied in ERISA Section 402(b)(4), on the basis of an IRS determination to defer effectiveness of a ruling under Section 401(a) of the Internal Revenue Code, a result which raises a separate question for review. See, *infra*, pp. 21-23.

for tax purposes;[11] but, under the Seventh Circuit ruling in this case, there is nothing which would prevent defined contribution pension plans, nonqualified defined benefit plans or employee welfare benefit plans from leaving the basis of benefit payments to the discretion of the employer.[12]

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[11] The IRS position has been effectively espoused by Congress in the Retirement Equity Act of 1984, Pub. L. 98-397, which added a new paragraph (25) to Section 401(a) of the Internal Revenue Code, expressly requiring that, in order to be a qualified plan, the actuarial assumptions utilized by a defined benefit plan must be "specified in the plan in a way which precludes employer discretion," 26 U.S.C. § 401(a)(25), as amended.

[12] While the issue in this case arises in the specific context of changes in actuarial assumptions, the potential for disruption of the statutory system of protections if Section 402(b)(4) is interpreted as tolerating employer discretion goes far beyond that limited context. For example, under the court of appeals' ruling, a plan which provides a defined benefit in accordance with a benefit formula based on years of participation in the plan could provide that the employer shall, from time to time, determine the definition of a "year of participation", subject only to the provisos that the definition must be reasonable and consistently applied to all participants, and that some credit must be given for each year in which the participant has at least 1000 hours of service. The provisos are the only limitations imposed on employer discretion by Section 204(b)(3) of ERISA and regulations thereunder. Pursuant to such a plan provision, an employer could, after a number of years of crediting employees with a full year of participation for each 1000-hour year, elect to redefine "year of participation" to require 2000 hours of service for a full year's credit, giving employees with more than 1000 hours of service but less than 2000 a partial year's credit on a pro-rata basis. The new definition is one which is specifically stated to be "reasonable and consistent" in Department of Labor Regulations § 2530.204-2(c)(4)(i), 29 C.F.R. § 2530.204(c)(4)(i). Under the ruling of the court below, there would be no violation of Sections 204(g) or 402(b)(4) of ERISA, even though the redefinition would dramatically and retroactively reduce the benefit entitlements already accrued of employees unable to meet the new 2000-hour test.

B. Whether the term "plan" in ERISA must be construed broadly to include all rules which determine participants' benefits, even if those rules are established by a legally permissible exercise of employer discretion and even if the rules are omitted from the formal plan document.

Setting aside for the moment the question of whether Section 402(b)(4) of ERISA requires the inclusion of the actuarial assumptions in the formal plan document in a manner precluding employer discretion, the issue in this case is *whether, for purposes of Section 204(g), the Plan includes rules which are not contained in the formal plan document*, so that a change in those rules constitutes a "plan amendment" subject to Section 204(g). The issue is not, as the court of appeals apparently thought, what the term "amendment" means. The issue is whether the interest rate changed by American was part of the Plan.

The court of appeals' approach is wholly inappropriate for broad remedial legislation such as ERISA.[13] The court construed the term "plan" narrowly, even though a broad interpretation is required by familiar principles of construction applicable to remedial statutes. A liberal interpretation of the term "Plan" to include all the rules, regulations and

[13] ERISA is a comprehensive remedial statute designed to protect plan participants. *See, e.g., Duchow v. New York State Teamsters Conference Pension & Retirement Fund*, 691 F.2d 74, 76 (2d Cir. 1982), *cert. denied*, 461 U.S. 918 (1983). Remedial legislation is to be liberally and broadly construed to effectuate the evident purpose of the statute, *Tcherepin v. Knight*, 389 U.S. 332, 336, 19 L.Ed.2d 564, 569 (1967), in favor of those intended to be benefitted, *Wirtz v. Titi Peat Humus Co.*, 373 F.2d 209 (4th Cir.), *cert. denied*, 389 U.S. 834 (1967), and in a manner tending to discourage attempted evasion by wrongdoers, *Westinghouse Electric Corp. v. Pacific Gas & Electric Co.*, 326 F.2d 575, 580 (9th Cir. 1964). Exceptions are to be narrowly construed and the burden of establishing an exception is on the party claiming it. *Weeks v. Southern Bell Telephone & Telegraph Co.*, 408 F.2d 228, 232 (5th Cir. 1969).

provisions having a material impact upon the determination of participants' rights and benefit entitlements, whether written or unwritten or found in the formal plan document or in some other document, is consistent with the statutory purpose. The narrow interpretation of the court below facilitates evasion of essential statutory safeguards.

In light of the purpose of ERISA to protect pension benefits from loss or reduction at the employer's discretion, these familiar principles militate against acceptance of a narrow interpretation of the term "plan". Under the court of appeals' interpretation, American was able to reduce petitioners' "accrued benefits" solely *because* it did not include the actuarial assumptions in the formal Plan document.

Under § 3(2) of ERISA, the term "plan" includes all rules affecting the rights and benefits of participants, whether written or unwritten. That Section defines the term pension plan as

> any plan, fund, or program which was heretofore or is hereafter established or maintained by an employer . . . to the extent that by its express terms or as a result of surrounding circumstances such plan, fund or program (i) provides retirement income to employees, or (ii) results in a deferral of income by employees for periods extending to the termination of covered employment or beyond . . .

The definition thus includes *any* plan, fund or program, not merely any *written* plan, fund or program as the court of appeals would have it. Indeed, the definition expressly authorizes reference to "surrounding circumstances" in ascertaining the content of a plan. If it were true that "plan" means only the written instrument, as American contended, Section 402(a), which requires that every *plan* be maintained "pursuant to a *written instrument*", becomes redundant.[14]

[14] Of course, failure to reduce the salient features of the plan to writing—even if American and the court of appeals were

(footnote continued on next page)

If the term "plan" were confined to those provisions which the sponsoring employer sees fit to include in the formal plan document, a fair reading of Section 402 would compel the conclusion that the actuarial assumptions *must* be included in it. Section 402(b)(4) requires that the "plan" specify the basis on which payments are to be made from the plan. The basis for optional forms of benefit payments is, in addition to the normal benefit formula based on years of service and compensation, the actuarial mortality and interest assumptions used to determine equivalence (Dk. No. 196, ¶ 5(a)). Having in mind the purpose of Section 402 (*See, supra* p. 14), to assure that plan participants be provided a written document containing all the information they require to determine their rights, inclusion of actuarial assumptions is clearly essential. Without those assumptions, *it is impossible for a participant to determine,* even with the assistance of a professional, *the amount of his benefit entitlement under any optional form.*

Despite the court's disclaimer, the only possible reading of the decision below is that "plan" means "formal plan document". Aside from being erroneous, such a conclusion has ramifications which undercut the basic protections ERISA was intended to provide. If the court had properly interpreted "plan" to include all rules affecting the rights and

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entirely correct that "plan" means only "written plan" and that Section 402(a) of ERISA is a mere tautology—would bring into play the final sentence of ERISA Section 3(2)(a) which provides:

> In the case of any arrangement or payment a principal effect of which is the evasion of the standards or purposes of this Act applicable to pension plans, such payment or arrangement shall be treated as a pension plan.

Furthermore, there are repeated references in the statute which assume that a "plan" may comprise a multiplicity of documents. *E.g.*, ERISA Sections 104(b)(2), 404(a)(1)(D), 29 U.S.C. §§ 1024(b)(2). 1104(a)(1)(D).

entitlements of participants, whether or not contained in the formal plan document, then the discount interest assumption used to calculate the lump-sum option, which was not contained in the formal Plan document, would have had to be viewed as part of the Plan. Since the assumed interest was changed from a fixed to a variable rate, that change in the *basis* of making payments from the Plan should have been found to require a plan amendment.

Petitioners do not ask that this Court close the historical loophole which the court below apparently thought existed (but which did not exist in fact); Congress has done that by *clarifying* the law in the Retirement Equity Act of 1984. *See supra* notes 9 and 11. Rather petitioners ask this Court to decide the meaning of a basic concept embodied in ERISA and to assure the effectiveness of ERISA's protections. Absent action by this Court correcting the Seventh Circuit's narrow, grudging and erroneous interpretation of the term "plan", employers may be able to contrive other imaginative ways to circumvent ERISA's substantive requirements.

C. Whether the IRS, in exercising its authority to delay the effectiveness of tax provisions in order to preserve an employer's tax deduction can relieve the employer of the duty to comply with parallel pre-existing substantive provisions of ERISA.

The fact that in 1979 the IRS gave existing pension plans until 1984 to comply with the requirement under the Internal Revenue Code that actuarial assumptions be included in the formal Plan document served only to preserve defendant American's tax deductions under Section 404 of the Internal Revenue Code; it did not—*and could not*—create a loophole relieving American of its fiduciary obligations to Petitioners and other Plan participants under the substantive provisions of Title I of ERISA.

The principal justification advanced by the court of appeals for not requiring the actuarial assumptions to be

included in the formal Plan document and for not considering them to be part of the Plan is that, the Internal Revenue Service, in Revenue Ruling 79-90, 1979-1 C.B. 155, delayed the effectiveness of Section 1.401-1(b)(1)(i) of its Regulations, requiring that such assumptions be included in the written instrument embodying the plan, until 1984 for plans in existence on March 12, 1979. Thus, since the American Plan was in existence on that date, the court found that American was not required to incorporate the actuarial assumptions into the Plan document until 1984.

In its administration of the tax laws, the IRS has authority under Section 7805(b) of the Code to defer or postpone the effectiveness of any of its determinations or rulings, including rulings relating to the conditions of continued tax-qualified status of pension plans (Sections 401 and 411) and the deductibility of employer contributions to such plans (Section 404). *But the IRS has no authority* to suspend or delay the effectiveness of non-tax laws governing the duties of plan fiduciaries.

The effectiveness of Section 402 of ERISA is expressly provided in Section 414 of ERISA. Under the latter section, Part 4 of subtitle B of Title I of ERISA—which includes Section 402—became effective on January 1, 1975. The IRS has no authority to defer the effectiveness of Section 402; that authority is conferred instead upon the Secretary of Labor, and the Secretary's authority is limited to postponements not extending beyond January 1, 1976. Thus, Section 402 of ERISA became effective with respect to the Plan on January 1, 1976, at the very latest. Since Section 402 of ERISA, properly interpreted, requires inclusion of the actuarial assumptions in the written instrument pursuant to which the Plan is maintained, and since that requirement is independent of the similar requirement under Section 1.401(b)(1)(i) of the IRS Regulations, the IRS could not postpone the substantive requirements of Section 402. Accordingly, the "loophole" relied upon by American and sanctioned by the court of appeals simply does not exist.

While the postponed effectiveness of Revenue Ruling 79-90 preserved defendant American's tax deduction, it could not alter American's obligations to its employees.

Petitioners cited Revenue Ruling 79-90 because it embodied the authoritative IRS interpretation of the Code analog to ERISA § 402(b)(4). As such, the Ruling represents persuasive, albeit nonbinding, authority for the proper interpretation of the substantive ERISA provision. The court below, satisfied with its restrictive interpretation of the term "amendment" in Section 204(g), never even addressed the question of the proper interpretation of Section 402(b)(4), except to reject petitioner's proferred interpretation solely on the grounds that the IRS had deferred the effectiveness of Revenue Ruling 79-90. This case therefore presents important questions as to the proper interplay between IRS interpretations of Code provisions and regulations, and the construction of parallel substantive provisions of ERISA, as well as to the extent of the IRS' authority to postpone effectiveness of those substantive provisions.

II.

There Is A Conflict Among the Circuits Which Can Be Effectively Resolved Only By this Court

The narrow interpretation of "plan" by the Seventh Circuit conflicts with decisions of other courts of appeals which have considered the meaning of the term "plan" in Section 3 of ERISA. Those courts have concluded that a "plan" is not simply the formal plan document and that the term is not limited to the formal written instrument required by Section 402 of ERISA.

Donovan v. Dillingham, 688 F.2d 1367 (11th Cir. 1982), involved a multiple employer trust established to allow small employers to secure group health insurance coverage for their employees at rates more favorable than those directly available to individual employers. The Secretary of

Labor sued the trustees seeking to establish that they were fiduciaries subject to ERISA fiduciary standards; the defendant trustees responded with the contention that the arrangements in question involved "only the bare purchase of insurance" and were not employee benefit plans subject to ERISA. In reversing the district court's dismissal of the action for want of jurisdiction, the Eleventh Circuit, in a unanimous *en banc* decision, held that ERISA reaches any plan, whether or not there is a formal written instrument, that it is proper to infer essential provisions of the plan from sources outside the plan document, and that the failure of the responsible plan fiduciaries to comply with Section 402 of ERISA did not relieve them from their duties and obligations under Title I of ERISA. 688 F.2d at 1372-73. *Accord, Scott v. Gulf Oil Corporation*, 754 F.2d 1499, 1503-04 (9th Cir. 1985).

In *Dependahl v. Falstaff Brewing Corp.*, 491 F. Supp. 1188 (E.D. Mo. 1980), *aff'd in relevant part* 653 F. 2d 1208 (8th Cir.) *cert denied*, 454 U.S. 968 (1981), the issue was whether a split-dollar insurance program covering key executives was an employee benefit plan. The employer argued that the program did not constitute an employee benefit plan because there was no *single* written document embodying the program as required by Section 402(a). The court responded:

> Defendants miss the point. If the CBS Plan falls within ERISA, as this court concludes that it does, defendants may not avoid the requirements of the Act by merely failing to comply and then arguing that the Plan is not within the Act due to their noncompliance. 491 F.Supp. at 1195.

Both *Donovan* and *Dependahl* interpreted the ERISA Section 3(1) definition of "welfare benefit plan" rather than the Section 3(2) definition of "pension benefit plan" involved here. But the two types of plans are simply subcategories of "employee benefit plan" or "plan" and are distinguished only by the character of the benefits provided. Thus both *Donovan* and *Dependahl* stand for the proposition that the

term "plan" as defined in Section 3 of ERISA is not merely synonymous with the written instrument, if any, embodying the plan as required by Section 402(a). The *Donovan* and *Dependahl* courts reached their conclusions from the explicit words of the statute and from a conviction that any other construction would subvert the statutory purpose. Significantly, Section 204(g) deals with amendments to the "plan", not amendments to the "written instrument".[15]

The Seventh Circuit did not cite either *Donovan* or *Dependahl*. Instead it relied on an inapposite decision, *Stewart v. National Shopmen Pension Fund*, 730 F.2d 1552 (D.C. Cir. 1984), *cert. denied*, 105 S.Ct. 127 (1984), apparently for the proposition that an action taken by a plan administrator pursuant to an express delegation of discretionary authority under the formal plan document does not constitute an

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[15] It is interesting to note that, in H.R. 2, the version of the act as it passed the House of Representatives, Section 3(2) would have provided:

> The term "employee pension benefit plan" or "pension plan" means any plan, fund or program *which is communicated or its benefits described in writing to the employees, and* which was heretofore or hereafter established or maintained by an employer . . . (III *Legislative History of the Employee Retirement Income Security Act of 1974 Prepared by the Subcommittee on Labor of the Senate Committee on Labor and Public Welfare*, 3904 (94th Con. 2d Sess. 1976)). (Emphasis added.)

And Section III(a)(1) of the House bill, the House version of the provision which ultimately became Section 402(a) of ERISA, read:

> Every employee benefit plan shall be established pursuant to a *written plan* . . . (*Id.* at 3947.)

Thus, the Act as it ultimately emerged from the Conference Committee purged all reference to any requirement of a writing from Section 3(2) and refined the language of Section 402(a) to maintain the distinction between a "plan" and the "*written instrument*" embodying it.

"amendment" of the plan. Since Section 402(b)(4) requires that the actuarial assumptions be stated in the plan document and not be left to the discretion of the plan administrator, the *Stewart* decision is simply irrelevant, even if the case actually stood for the principle claimed.

In *Stewart*, the plan in question, unlike the American Plan, was a multi-employer plan which contained a provision—*expressly authorized by Section 203(a)(3)(E) of ERISA in order to avoid "dumping" of unfunded liabilities on multi-employer plans by withdrawing employers*—which permitted the plan trustees to cancel participants' credits for services attributable to service prior to the date their particular employer joined the plan and began making contributions. In other words, when a new employer entered the plan, his employees were conditionally granted credit for pre-participation years of service in calculating their benefit entitlement, subject to cancellation if their employer later withdrew and stopped making contributions. When the *Stewart* plaintiffs' employer ceased making contributions, the trustees exercised their authority to cancel credits for pre-participation years of service.

The court held that this exercise of the trustees' authority did not entail any "amendment to the vesting schedule" subject to Section 203(c)(1)(A) since the plaintiffs retained an unqualified right to receive a benefit. The court also held that the action did not violate Section 204(g) since it did not have the effect of amending the plan. This latter ruling was clearly correct under the circumstances; the service credits in question had always been conditioned on the employer's continued contributions and since the interpretation sought by the *Stewart* plaintiffs would have effectively repealed Section 203(a)(3)(E). Not only were the cancellations specifically authorized by the statute, in consequence of Congressional recognition of the special problems of multi-employer pension plans,[16] but they were implemented by the trustees

[16] Section 203(a)(3)(E) was added to ERISA by Section 303 of the Multi-employer Pension Plan Amendments Act of 1980, Publ. L. 96-364. Among the findings leading to enactment of

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in specific, narrowly-delineated circumstances, affected only particular participants and, as the court held, were still subject to judicial scrutiny to assure that the action was not arbitrary or capricious in relation to the statutory purpose of permitting cancellation of pre-participation service by multi-employer plans. Such considerations are not applicable to single employer plans such as the American Plan.

Moreover, even ignoring the dangers of relying on decisions involving multi-employer plans in the single employer context, there is a qualitative difference between the action taken by the *Stewart* trustees and the conduct involved in this case. In the *Stewart* case, the plan expressly authorized cancellation of service credits in particular circumstances. The cancellation therefore did not alter the plan provisions (whether those provisions were contained in the formal document or otherwise), did not change the rates at which benefits accrued under the plan, and affected only the employees of the withdrawing employer. Here, the action of American changed the assumptions in a manner which affected every active participant and all past benefit accruals. In short, American changed a rule of general application under the Plan, whereas the *Stewart* trustees merely applied a pre-existing rule to the specific facts of the case before them. Whether the actuarial assumptions changed by the American administrator were or were not part of the Plan—the real issue in the present case—is something upon which the *Stewart* decision sheds no light.

Although it ignored *Donovan* and *Dependahl*, the court's decision is in conflict with them.

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that Act was the determination of Congress that "withdrawals of continuing employers from a multi-employer pension plan frequently result in substantially increased funding obligations for employers who continue to contribute to the plan, adversely affecting the plan, its participants and beneficiaries, and labor relations." (P.L. 96-364, § 3(a)(4)(A)).

CONCLUSION

For the foregoing reasons, the petition for certiorari should be granted.

Respectfully submitted,

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November 1, 1986

APPENDIX A
(Opinions and Judgments Below)

In the

United States Court of Appeals

For the Seventh Circuit

No. 85-1830

ROY E. DOOLEY, JR., et al.,

Plaintiffs-Appellants,

v.

AMERICAN AIRLINES, INC.,

Defendants-Appellees.

Appeal from the United States District Court
for the Northern District of Illinois, Eastern Division.
No. 81 C 6770—**James B. Parsons**, *Judge*.

ARGUED FEBRUARY 27, 1986—DECIDED AUGUST 5, 1986

Before WOOD, JR., FLAUM and RIPPLE, *Circuit Judges*.

RIPPLE, *Circuit Judge*. The appellants, retired pilots of American Airlines, brought this four count complaint pursuant to the Employee Retirement Income Security Act (ERISA). They sought to enforce their rights under an American Airlines defined benefit pension plan. The district court, on cross-motions for summary judgment, held that the alleged ERISA violations were unfounded. Accordingly, the court entered judgment in favor of the appellees on all four counts. While we agree with the district court's disposition of Count I, we disagree with its disposition of Counts II through IV. Therefore, we affirm the district court's judgment in part, and we reverse that judgment in part and remand this case for further proceedings.

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I

This is an action brought under the Employee Retirement Income Security Act (ERISA), 29 U.S.C. § 1132(a), to recover benefits and enforce rights under the terms of the American Airlines, Inc. Fixed Income Plan of the Pilot Retirement Income Program (Plan). The plaintiffs-appellants are fifty-eight retired pilot employees for American Airlines (Pilots). The defendants, all of whom are sued in their capacity as ERISA-defined fiduciaries, include 1) American Airlines, Inc., 2) the Plan, and 3) five individual members of American's Pension Benefits Administration Committee (collectively American).

The Plan is a "defined benefit pension plan" which provides that, upon retirement at age 60, a pilot employee is entitled to receive a Basic Retirement Annuity consisting of a monthly pension equal to 1.25% of the employee's final average compensation multiplied by a number equal to one less than the number of years of the employee's credited service. Reduced to its essentials, this means that an employee is entitled to receive a monthly annuity-like payment from the Plan. However, at the time of this litigation, a pilot employee was not *required* to receive his retirement in the usual annuity form. Instead, pilot employees were also entitled, pursuant to section 10.4 of the Plan, to select payment in one of a number of optional forms. This litigation focuses on the Plan's administration of only one of section 10.4's optional payment plans.

In this case, the Pilots chose to receive their retirement benefits in the form of a lump-sum payment. While that option was not specifically provided for in the actual plan document, payments in that form were nonetheless authorized by the document. Section 10.4(c) of the Plan provided:

> (c) *Open Option*. A member may elect, if the Administrator consents thereto on the basis of policies uniformly applicable to all Members similarly situated, to receive his or her Basic Retirement Annuity . . . in an optional form other than one specifically provided in this Section. . . .

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Appellants' Br. at 6. Pursuant to this section, American Airlines issued Bulletin No. 547-78 on October 26, 1978. That Bulletin provided that American Airlines:

> and the Allied Pilots Association have agreed to allow lump-sum distributions at retirement from the Pilot Retirement Benefit Plan. This form of payment would be granted under the Open Option and is offered in addition to the various forms of payment currently provided under the Plan.

R.85, Ex. B. The Bulletin continued by explaining a number of preconditions to an employee's acceptance of payments under the lump-sum option. Furthermore, and more importantly for our purposes, the Bulletin also specifically stated that:

> Distributions will be based on the annual benefit otherwise provided under the Plan multiplied by a lump-sum annuity factor. The factor is developed using an 8½% interest rate and the 1971 Group Annuity Mortality Table.

Id. Thus, at its inception, the lump-sum option had a stated 8½% fixed actuarial assumption. That assumption was used to discount to present value the total amount of payments that an employee would have otherwise received if he had selected the annuity option.

The fixed-rate actuarial assumption remained in effect for slightly more than one year. Then, on December 26, 1979, American Airlines issued Bulletin No. 497-79 which discontinued the fixed rate and, instead, adopted a floating actuarial assumption computed as 1% greater than the Moody's AAA Corporate Bond Rate for the second month preceding the employee's retirement date.[1] R.85, Ex. D. According to the Bulletin, "[t]he purpose of this revision

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1 This change came just ten months after the Internal Revenue Service issued Rev. Rul. 79-90, 1979-1 C.B. 156. That Ruling informed pension plans that their actuarial assumptions must be specified in the plan itself.

[was] to conform such interest rate to currently prevailing interest rates and to the Company's expectation for return on investment of pension assets for the intermediate term, that is, the term over which the series of payments would be made." *Id.* Shortly thereafter, this new policy was slightly modified. In Bulletin No. 161-80, issued on April 22, 1980, American Airlines 1) altered some of the preconditions for lump-sum payment, 2) changed the relevant Moody's AAA Corporate Bond Rate from the second to the third month preceding the employee's retirement, and 3) initiated a policy of "phasing in" the new floating rate by upwardly adjusting the 8½% fixed rate by 2% each month until it overtook the "Moody's + 1" rate. R.85, Ex. E.

The dispute in this case centers on American Airlines' change in the actuarial assumption from the 8½% fixed rate to the "Moody's + 1" floating rate. According to the Pilots, between February 1981 and October 1982 the relevant Moody's rate ranged from a low of 12.12% to a high of 15.49%; therefore, the "Moody's + 1" rate peaked at a high of 16.49%. Appellants' Br. at 8. Because of this shift in interest rate, retirees during this period received a much smaller lump-sum payment than those individuals who retired while the 8½% fixed rate was still in effect. As a result, the Pilots brought this four count action in the district court. Count I asserts that American's change to the floating interest assumption constituted an amendment to the Plan which resulted in a reduction of accrued benefits in violation of ERISA § 204(g), 29 U.S.C. § 1054 (g).[2] Count II asserts, in the alternative, that the floating interest rate was unreasonably high during the relevant time period and, therefore, resulted in lump-sum benefits which were less than actuarially equivalent to the normal retirement annuity. This deficiency, according to the

[2] ERISA § 204(g), 29 U.S.C. § 1054(g), then provided:

The accrued benefit of a participant under a plan may not be decreased by an amendment of the plan, other than an amendment described in section 1082(c)(8) of this title.

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appellants, created a violation of the vesting provisions of ERISA § 203, 29 U.S.C. § 1053.[3] Count III is premised on the theory that 1) increases in the interest assumption lead to reductions in lump-sum benefits, and 2) reductions in lump-sum benefits lead to substantially smaller contributions to the Plan on the part of the employer, American Airlines. Given these linkages, Count III alleges that the change in the actuarial interest rate assumption was motivated by the Plan fiduciaries' desire to benefit economically American Airlines in violation of ERISA § 404(a)(1)(A), 29 U.S.C. § 1104(a)(1)(A),[4] which requires fiduciaries to discharge their duties solely in the interest of the Plan's participants and beneficiaries. Finally, Count IV seeks injunctive relief to prevent the continuation of the activities alleged in the previous three counts.

The district court, ruling on the Pilots' motion for summary judgment on Count I and American's cross-motion for summary judgment on Counts I through IV, found in favor of the defendants. The district court held that:

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[3] ERISA § 203, 29 U.S.C. § 1053, provides, in part:

Each pension plan shall provide that an employee's right to his normal retirement benefit is nonforfeitable upon the attainment of normal retirement age and in addition shall satisfy the requirements of paragraphs (1) and (2) of this subsection.

(1) A plan satisfies the requirments of this paragraph if an employee's rights in his accrued benefit derived from his own contributions are nonforfeitable.

[4] ERISA § 404(a)(1)(A), 29 U.S.C. § 1104(a)(1)(A), provides:

(1) Subject to sections 1103(c) and (d), 1342, and 1344 of this title, a fiduciary shall discharge his duties with respect to a plan solely in the interest of the participants and beneficiaries and—

(A) for the exclusive purpose of:

(i) providing benefits to participants and their beneficiaries; and

(ii) defraying reasonable expenses of administering the plan.

> The Plan in question specifically provides that any alternative form of payment must be "actuarially equivalent" to a retiree's Basic Retirement annuity. "Actuarially equivalent" is defined in the Plan as "the equivalent in value on the basis of actuarial factors approved from time to time by American Airlines."
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> * * *
>
> [Therefore, the] defendants' change in the discount interest rate did not constitute a "plan amendment" under ERISA and did not cause an unlawful reduction in plaintiffs' retirement benefits.

Dooley v. American Airlines, Inc., No. 81 C 6770, slip op. at 5-6 (N.D. Ill. Apr. 17, 1985) [hereinafter Order]. Relying on this basis, the district court found for the defendants on Count I. The court continued by stating:

> The Plan required that the lump sum payment be actuarially equivalent to the retirees' Basic Retirement annuity. The defendants' action served to insure actuarial equivalence. Accordingly, the defendants are not guilty of violating their fiduciary duties. Rather, I find that the defendants exercised good judgment in instituting the variable rate which will provide actuarial equivalence between available options.

Id. at 6. Based on these findings, the district court also found for American on Counts II and III. Additionally, since Count IV was derivative of the other three counts, and since the other three had been resolved in favor of American, the district court found in favor of American on Count IV. This appeal followed.

II

A. COUNT I

Count I deals with the alleged violation of ERISA § 204(g), 29 U.S.C. § 1054(g).[5] That statute provides, in pertinent

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[5] In 1984, section 204(g) was amended by adding the following language:

(Footnote continued on following page)

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part, that "[t]he accrued benefit of a participant under a plan may not be decreased by an amendment of the plan. . . ." Thus, the essential elements of a section 204(g) violation are: 1) a plan amendment, and 2) a reduction in accrued benefits. Since we agree with American that no plan amendment occurred in this case, we need not reach—and voice no opinion concerning—whether, if there were a plan amendment in this case, it would have served to reduce an employee's accrued benefits.

American contends that, assuming that the actuarial assumptions in this case can be construed as part of the employee benefit plan,[6] there was no ERISA § 204(g) violation because there was no plan amendment. To support this position, American first refers this court to the ac-

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[5] *continued*

For purposes of [the preceding] paragraph . . ., a plan amendment which has the effect of—

(A) eliminating or reducing an *early retirement benefit* or a retirement-type subsidy (as defined in regulations), or

(B) eliminating an *optional* form of benefit,

with respect to benefits attributable to service before the amendment shall be treated as reducing accrued benefits. In the case of a retirement-type subsidy, the preceding sentence shall apply only with respect to a participant who satisfies (either before or after the amendment) the preamendment conditions for the subsidy. The Secretary of the Treasury may by regulations provide that this subparagraph shall not apply to a plan amendment described in subparagraph (B) (other than a plan amendment having an effect described in subparagraph (A)).

29 U.S.C. § 1054(g) (emphasis added). This amendment became effective for plan years beginning after December 31, 1984—well after the relevant time period in this case. Therefore, the amendment has no direct relationship on the result of our case.

[6] The parties have briefed and argued whether the actuarial assumptions—contained, as they were, in bulletins which were physically distinct from the pension plan document—can be construed as part of the pension plan for purposes of ERISA. Because of our disposition of this case, we need not reach that question.

tual pension document. Section 10.4 of the plan—the section under which the lump-sum payment was authorized—stated: "Any optional form of Basic Retirement Annuity elected pursuant to this Section shall be the Actuarial Equivalent of an annuity payable for the lifetime of the Member only in an annual amount equal to such Basic Retirement Annuity. . . ." Thus, section 10.4 can be fairly read as imposing a requirement that all optional forms of pension payments must be actuarially equivalent to the standard annuity form of payment. Additionally, Article II of the pension document (the article which defines the terms which will be used throughout the document) defines "actuarial equivalent" as "the equivalent in value on the basis of actuarial factors *approved from time to time by American Airlines. . . .*" Article II, § (d) (emphasis added). Therefore, by putting both of these provisions together, American contends that the pension plan administrators—by changing the actuarial assumption from the 8½% fixed rate to the "Moody's + 1" floating rate—were merely exercising a provision *which was already in the pension plan.* Accordingly, there could be no "plan amendment" because the administrators were merely carrying-out the provisions of the plan as it then stood.

American has supplied case law support for its position. In *Stewart v. National Shopmen Pension Fund,* 730 F.2d 1552 (D.C. Cir. 1984), the District of Columbia Circuit discussed the appropriate meaning of "plan amendment." Dealing with ERISA §§ 203(c)(1)(B) and 204(g), the court noted that:

> In both sections, the word "amendment" is used as a word of limitation. Congress did *not* state that any change would trigger the two provisions; it stated that any change *by amendment* would do so. The district court found, and the plaintiffs admit, that there was no "amendment" to the plan in the "technical" sense—*i.e.*, an actual change in the provisions of the plan. True. All that happened was that § 2.09, a provision already incorporated into the plan, was *applied.* Actions authorized by the plan were carried out by the persons authorized to do so.

730 F.2d at 1561 (emphasis in original). In *Stewart*, the court was faced with a multi-employer pension fund. That pension fund specifically provided that if an employer's participation in the fund should terminate, the fund's trustees were empowered to cancel any portion of an employee's pension which was based on the employee's service with that particular employer prior to the time that the employer joined the multi-employer fund.[7] While the *Stewart* decision is factually distinguishable from the present case, its commonsensical rule of law is nonetheless applicable here. In the context of this particular pension plan, the plan fiduciaries had the authority to change the actuarial assumptions "from time to time" in an effort to maintain actuarial equivalence. That is precisely what they did in this case. Therefore, we are unwilling to contort the plain meaning of "amendment" so that it includes the valid exercise of a provision which was already firmly ensconced in the pension document.

In rebuttal, the Pilots argue that the Plan, by allowing this type of employer discretion in the setting of actuarial assumptions, was violative of ERISA. Therefore, they contend that we should disregard the Plan's discretionary provision as a matter of public policy. In this respect, the Pilots place their primary reliance on ERISA § 402(b)(4), 29 U.S.C. § 1102(b)(4), and Internal Revenue Code § 401 (IRC § 401), 26 U.S.C. § 401.

ERISA § 402(b)(4) provides that: "Every employee benefit plan shall—(4) specify the basis on which payments are made to and from the plan." Similarly, Treasury Regulation 1.401-1(b)(1)(i) requires that, for a plan to be qualified

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[7] Notably, such a provision is both contemplated by and specifically approved of in ERISA. *See* ERISA § 203(a)(3)(E), 29 U.S.C. § 1053(a)(3)(E). The *Stewart* court recognized this point when it stated: "To give trustees the flexibility necessary for efficient operation of pension funds, Congress has recognized and provided for several situations in which plans can reduce or eliminate benefits to participants by implementing preexisting plan provisions." 730 F.2d at 1563 (footnote omitted).

under IRC § 401, the plan must provide for "definitely determinable benefits." This latter requirement is met when the level of employee benefits is computed via a fixed formula and "*is not within the discretion of the employer.*" *See* Rev. Rul. 74-385, 1974-2 C.B. 130. Accordingly, since IRC § 401's "definitely determinable benefits" requirement is, in some respects, parallel to the ERISA § 402(b)(4) requirement (plan must specify the basis upon which payments are to be made), the Pilots would like to incorporate into ERISA, by analogy, the decisions under IRC § 401 which prohibit employer discretion in the establishment of employee benefit computational formulae.

Specifically, the Pilots would like to rely on Rev. Rul. 79-90, 1979-1 C.B. 156. That ruling, issued to explain the "definitely determinable benefits" requirement of Reg. 1.401-1(b)(1)(i), provides:

> Whenever the amount of a benefit in a defined benefit plan is to be determined by some procedure (such as "actuarial equivalent", "actuarial reserve", or "actuarial reduction") which requires the use of actuarial assumptions (interest, mortality, etc.) *the assumptions to be used must be specified within the plan in a manner which precludes employer discretion.*

(Emphasis added.) Therefore, to qualify as an IRC § 401 pension, a plan must eliminate employer discretion from the establishment of its actuarial assumptions. The Pilots would like us to impose this obligation on American Airlines. We decline the Pilots' invitation to take this step.

Since the IRS believed that Rev. Rul. 79-90 was a novel decision, the IRS devised a plan for phasing-in its effectiveness. For pension plans in existence on March 12, 1979 (the date of Rev. Rul. 79-90), the Ruling would first become effective for plan years beginning on or after December 31, 1983. For plans which were not in existence on March 12, 1979, the Ruling would become immediately effective. Finally, even if a plan's existence pre-dated March 12, 1979, if that plan already included its actuarial assump-

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tions (i.e.: if the plan unwittingly complied with the revenue ruling) those assumptions could *not* be removed.

There can be no question either that the Plan was in existence on March 12, 1979 or that, on that date, the Plan was not in compliance with the employer discretion prohibitions contained in Revenue Ruling 79-90. Furthermore, there is no doubt that the IRS gave non-complying pension plans until December 31, 1983—well after the relevant time frame in this case—to come into compliance with its new ruling. Given this grace period, and given the fact that the IRS' section 401 treasury regulations and revenue rulings are neither incorporated into ERISA, *see* 29 U.S.C. § 1202(c), nor binding on us in this situation, *see* *Carle Foundation v. United States*, 611 F.2d 1192, 1195 (7th Cir. 1979), we see no reason to immediately impose upon American a provision with which it was given years to comply.

Accordingly, we affirm the decision of the district court insofar as it granted summary judgment for the appellees with respect to Count I.

B. COUNTS II THROUGH IV

Count II alleges that the new actuarial figure set by American Airlines (the "Moody's + 1" rate) did not, in fact, achieve actuarial equivalence and, therefore, violated ERISA § 203, 29 U.S.C. § 1053. Count III alleged that the pension plan's fiduciaries breached their duty by increasing the interest assumption in order that American Airlines (neither a plan participant nor a beneficiary) would be economically benefited. Both of these counts are closely related and both turn upon whether the plan fiduciaries appropriately set the new, floating-rate interest factor. In granting summary judgment in favor of the appellees on Counts II and III, the district judge apparently concluded that "[t]he defendants' action [in changing the interest assumption] served to insure actuarial equivalence." Order at 6. We believe that this factual finding was inappropriate given the summary judgment posture of this case.

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Summary judgment may be granted only if the record indicates "that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law." Fed. R. Civ. P. 56(c). As we stated in *Munson v. Friske*, 754 F.2d 683, 690 (7th Cir. 1985) (citations omitted):

> In reviewing a summary judgment, an appellate court must view the entire record and the inferences drawn therefrom in the light most favorable to the party opposing the motion. If a study of the record reveals that inferences contrary to those drawn by the trial court might be permissible, then the summary judgment should be reversed.

In this case, the appellants were able to raise a material issue of fact regarding the actuarial appropriateness of setting the interest assumption at the "Moody's + 1" rate. One of the appellants' experts, Mr. Carl H. Fischer, stated, as follows, in his affidavit:

> *Actuarial Equivalence of Lump Sum Distributions.* In my professional opinion, actuarial equivalence must be determined on the basis of reasonable actuarial assumptions, consistently applied, including a reasonable interest assumption. Reasonableness implies a range and there is, therefore, no single interest rate which, alone, constitutes the reasonable interest assumption for purposes of actuarial equivalence. In my opinion, during the period from February, 1981, through September, 1982, during which most of the plaintiffs retired:
>
> (a) 8½% was, and continued to be, well within the range of reasonable interest assumptions for purposes of determining the actuarial equivalence of lump sum distributions.
>
> (b) The highest reasonable interest rate for purposes of determining actuarial equivalence of lump sum distributions was the rate promulgated by the Pension Benefit Guaranty Corporation for valuing immediate annuities, which rate, during the period in question, ranged from a low of 9¾% to a high of 11%.

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(c) During a period of high volatility in market rates of interest, a variable interest rate, indexed to a standard intended to reflect current market rates of interest, with no provision for eliminating the extremes of the fluctuations through averaging or some other technique, does not provide a reasonable interest assumption for purposes of determining the actuarial equivalence of lump sum distributions.

(d) A variable interest rate, one percentage point greater than the Moody's Aaa Corporate Bond Rate for the third month prior to retirement, was not, during the period in question, a reasonable basis for determining actuarial equivalence of lump sum distributions under the American [Airlines] Plan.

R.106 at 33-34. In his deposition, Mr. Fischer also often repeated his belief that an interest assumption, in order that it accurately result in an actuarially equivalent amount in times of fluctuating interest rates, must incorporate some form of averaging which will moderate large, short-term changes in the current market interest rate. R.117, Ex. W at 12, 13, 20, 21, 22. This testimony provided sufficient evidence, especially in light of the rather incomplete record on this point, to create a disputed issue of material fact. Accordingly, we reverse the district court's grant of summary judgment on Counts II and III, and we remand this case for further record development and proceedings. Additionally, since Count IV (seeking injunctive relief against the conduct which forms the basis for Counts I through III) is closely related to and, in part, derivative of Counts II and III, we reverse the grant of summary judgment on that count also and we remand it along with the other two counts.[8]

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[8] We leave it to the district court to determine, in the first instance, whether any or all of the appellants' releases are valid and enforceable.

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III

In sum, we hold that summary judgment in favor of the appellees was appropriate with respect to Count I since there was no plan amendment. Accordingly, we affirm the district court's judgment with respect to Count I. However, with respect to Counts II through IV, we find that resolution of these three counts requires additional findings on a disputed issue of material fact. Therefore, we reverse the district court's grant of summary judgment and we remand this case for further proceedings. Each party will bear its own costs of this appeal.

AFFIRMED IN PART, REVERSED AND REMANDED IN PART.

A true Copy:

Teste:

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Clerk of the United States Court of Appeals for the Seventh Circuit

No. 81 C 6770

In the

United States District Court

FOR THE NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

ROY E. DOOLEY, JR., et al.,

Plaintiffs,

v.

AMERICAN AIRLINES, INC., et al.,

Defendants.

MEMORANDUM OPINION AND ORDER

Plaintiffs, who are 58 recently retired airline pilots, filed a four-count complaint against their former employer, American Airlines, Inc., its pilot pension plan, and the Plan fiduciaries to recover damages for an alleged illegal reduction of their lump sum pensions. Both parties are in agreement as to the pertinent facts. American Airlines administers a retirement benefit program for its pilots which consists of two plans, the Variable Income Plan and the Fixed Income Plan. When a pilot retires from American Airlines he is eligible to draw benefits from both Plans. Under the Fixed Income Plan, a retiring pilot is entitled to a lifetime annuity. The retiring pilot may elect to receive his payment as a joint and survivor annuity, a ten-year guaranteed payment, a "level income" payment or under an "open option". It was under the "open option" that the 58 plaintiffs elected to receive their benefits in a lump sum payment.

On October 26, 1978 the lump sum option was adopted. American Airlines notified its employees of the "lump sum" option through a bulletin which indicated that the lump sum

benefit would be a payment equal to the annual benefit yet multiplied by a lump sum annuity factor based on a discount interest rate of 8½% and the 1971 Group Annuity Mortality Table.

In December of 1979 American Airlines decided to change its formula for computing lump sum benefits. A second bulletin was posted on April 22, 1980 indicating that effective January 1, 1981, the Plan would use a variable interest rate to compute lump sums paid out of the Fixed Income Plan. The new rate would be a fluctuating rate calculated by adding an additional percentage point to the interest rate set by Moody's Aaa Corporate Bond Rate. The bulletin also indicated that there would be a phase-in period whereby commencing in February 1981 monthly increments of 2% would be added to the then existing rate of 8.5% until the Moody's-plus-one rate was reached.

Count I of plaintiffs' third amended complaint is brought under § 502(a)(1)(B) of ERISA. Specifically plaintiffs allege that the purpose and effect of defendant American Airlines' unilateral discontinuance of the 8½% interest assumption and substitution of a variable interest rate indexed to Moody Aaa corporate bond rate in computing lump sum distributions under defendants' Plan was to increase substantially the rate of interest used in determining the lump sum distribution entitlement of participants retiring on and after February 1, 1981. Plaintiffs further allege that as a result of the increased assumption, the aggregate dollar amounts of lump sum distributions to which participants of defendant Plan retiring on or after February 1, 1981 are entitled are substantially less than such participants would have received had such distributions continued to be computed on the basis of the 8½% interest assumption previously used. Plaintiffs assert that defendants' unilateral change in the interest assumption constituted an amendment to the Plan having the effect of decreasing the participants' accrued rights in violation of § 204(g) of ERISA, 29 U.S.C. § 1054(g).

Count II of plaintiffs' third amended complaint is brought under section 502(a)(1)(B) of ERISA (29 U.S.C. §§ 1132(a)(1)(B) as amended). In Count II plaintiffs assert that the interest assumption adopted by the defendants is unreasonably high and that as a result of the increased interest assumption, the lump sum distributions paid to participants of defendants' Plan retiring on and after February 1, 1981, including plaintiffs, are not actuarially equivalent to the Basic Retirement annuities such participants otherwise were entitled to receive. Plaintiffs therefore assert violations of defendants' Plan and section 203 of ERISA (29 U.S.C. 1053 as amended).

Count III of plaintiffs' third amended complaint is brought under sections 502(a)(2) and 409(a) of ERISA (29 U.S. §§ 1132(a)(2) and 1109(a)) as amended and alleges a breach of defendant American and individual defendants' fiduciary duties to defendant Plan, its participants and beneficiaries. Specifically plaintiffs allege that the change in interest assumption was conceived and implemented by defendants for the purpose of profiting defendant American through reduced contributions to the Plan in order to divert funds to its own corporate purposes.

Count IV of plaintiffs' third amended complaint is brought under section 502(a)(3) of ERISA (29 U.S.C. § 1132(a)(3) as amended) and seeks to enjoin defendants from implementing and enforcing the change in interest assumption or any other change in interest assumption which decreases accrued benefits against plaintiffs. Count IV also seeks attorney's fees and costs.

The motions which are currently before me are the motion of the plaintiffs for summary judgment on Count I of their third amended complaint and the cross-motion of the defendants for summary judgment on Counts I-IV of the plaintiffs' third amended complaint. The sole issue remaining in this case is a question of law which is appropriate for summary judgment. Specifically the question of law before

the court is whether defendants' conduct constituted a violation of ERISA.

The Plan in question specifically provides that any alternative form of payment must be "actuarially equivalent" to a retiree's Basic Retirement annuity. "Actuarially equivalent" is defined in the Plan as "the equivalent in value on the basis of actuarial factors approved from time to time by American Airlines." The maintenance of actuarial equivalence is an obligation imposed upon defendants by specific provisions of the Plan. Administrative changes in the interest rates are mandatory under the Plan and are the means of maintaining actuarial equivalence. As stated in *Grand Union Co. and Independent Transportation Employees Assoc.*, 82 ARB ¶8843 (June 2, 1982),

> When money can be invested at a higher rate of interest, it requires a smaller lump sum to fund a future stream of retirement benefits, and the fall of the lump sum option dollar amount was a "mathematical fact of life"—freezing the interest rate would have produced a lump sum windfall.

The administrators of the Plan were charged with the responsibility of acting for the benefit of all participants of the Plan. I am persuaded by defendants' memorandum and the United States District Court for the Northern District of Georgia Atlanta Division's decision in *Lewis v. Fulton*, No. C82-736A slip opinion (N.D. Ga. Aug. 31, 1983) that defendants' change in the discount interest rate did not constitute a "plan amendment" under ERISA and did not cause an unlawful reduction in plaintiffs' retirement benefits. I am not persuaded by plaintiffs' arguments regarding Revenue Rulings 79-90 1979-1 LB. 155 and 81-D, 1981-1 C.B. 228. I will adopt the findings of the Georgia District Court regarding these Revenue rulings.

I therefore find that defendants are entitled to summary judgment on Counts I-IV of plaintiffs' third amended complaint. The fact that the dollar amounts of the lump sum

option payments may have fallen as a result did not change the Plan or participants' rights under the plan. The Plan required that the lump sum payment be actuarially equivalent to the retirees' Basic Retirement annuity. The defendants' action served to insure actuarial equivalence. Accordingly, the defendants are not guilty of violating their fiduciary duties. Rather, I find that the defendants exercised good judgment in instituting the variable rate which will provide actuarial equivalence between the available options.

The plaintiffs' motion for summary judgment is hereby denied. The defendants' motion for summary judgment on Counts I-IV of the plaintiffs' third amended complaint is granted. It is so ordered.

ENTER:

James B. Parsons

April 17, 1985

APPENDIX B
(Statutes and Regulations Involved)

STATUTES INVOLVED

Section 3(1), (2) and (3) of the Employee Retirement Income Security Act of 1974, 29 U.S.C. § 1002(1), (2) and (3)

§ 1002. Definitions

For purposes of this subchapter:

(1) The terms "employee welfare benefit plan" and "welfare plan" mean any plan, fund, or program which was heretofore or is hereafter established or maintained by an employer or by an employee organization, or by both, to the extent that such plan, fund, or program was established or is maintained for the purpose of providing for its participants or their beneficiaries, through the purchase of insurance or otherwise, (A) medical, surgical, or hospital care or benefits, or benefits in the event of sickness, accident, disability, death or unemployment, or vacation benefits, apprenticeship or other training programs, or day care centers, scholarship funds, or prepaid legal services, or (B) any benefit described in section 186(c) of this title (other than pensions on retirement or death, and insurance to provide such pensions).

(2)(A) Except as provided in subparagraph (B), the terms "employee pension benefit plan" and "pension plan" mean any plan, fund, or program which was heretofore or is hereafter established or maintained by an employer or by an employee organization, or by both, to the extent that by its express terms or as a result of surrounding circumstances such plan, fund, or program—

> **(i)** provides retirement income to employees, or
>
> **(ii)** results in a deferral of income by employees for periods extending to the termination of covered employment or beyond,

regardless of the method of calculating the contributions made to the plan, the method of calculating the benefits

under the plan or the method of distributing benefits from the plan.

(B) The Secretary may by regulation prescribe rules consistent with the standards and purposes of this chapter providing one or more exempt categories under which—

(i) severance pay arrangements, and

(ii) supplemental retirement income payments, under which the pension benefits of retirees or their beneficiaries are supplemented to take into account some portion or all of the increases in the cost of living (as determined by the Secretary of Labor) since retirement,

shall, for purposes of this subchapter, be treated as welfare plans rather than pension plans. In the case of any arrangement or payment a principal effect of which is the evasion of the standards or purposes of this chapter applicable to pension plans, such arrangement or payment shall be treated as a pension plan.

(3) The term "employee benefit plan" or "plan" means an employee welfare benefit plan or an employee pension benefit plan or a plan which is both an employee welfare benefit plan and an employee pension benefit plan.

Section 204(g) of the Employee Retirement Income Security Act of 1974, 29 U.S.C. § 1054(g)

Prior to Amendment by Retirement Equity Act of 1984:

§ 1054

(g) The accrued benefit of a participant under a plan may not be decreased by an amendment of the plan, other than an amendment described in section 1082(c)(8) of this title.

Subsequent to Amendment by Retirement Equity Act of 1984:

§ 1054

(g) Decrease of accrued benefits through amendment of plan

(1) The accrued benefit of a participant under a plan may not be decreased by an amendment of the plan, other than an amendment described in section 1082(c)(8) of this title.

(2) For purposes of paragraph (1), a plan amendment which has the effect of—

> **(A)** eliminating or reducing an early retirement benefit or a retirement-type subsidy (as defined in regulations), or
>
> **(B)** eliminating an optional form of benefit,

with respect to benefits attributable to service before the amendment shall be treated as reducing accrued benefits. In the case of a retirement-type subsidy, the preceding sentence shall apply only with respect to a participant who satisfies (either before or after the amendment) the preamendment conditions for the subsidy. The Secretary of the Treasury may by regulations provide that this subparagraph shall not apply to a plan amendment described in subparagraph (B) (other than a plan amendment having an effect described in subparagraph (A)).

Section 402(a) and (b) of the Employee Retirement Income Security Act of 1974, 29 U.S.C. § 1102(a) and (b)

§ 1102. Establishment of plan

(a) Named fiduciaries

(1) Every employee benefit plan shall be established and maintained pursuant to a written instrument. Such instrument shall provide for one or more named fiduciaries who

jointly or severally shall have authority to control and manage the operation and administration of the plan.

(2) For purposes of this subchapter, the term "named fiduciary" means a fiduciary who is named in the plan instrument, or who, pursuant to a procedure specified in the plan, is identified as a fiduciary (A) by a person who is an employer or employee organization with respect to the plan or (B) by such an employer and such an employee organization acting jointly.

(b) Requisite features of plan

Every employee benefit plan shall—

(1) provide a procedure for establishing and carrying out a funding policy and method consistent with the objectives of the plan and the requirements of this subchapter,

(2) describe any procedure under the plan for the allocation of responsibilities for the operation and administration of the plan (including any procedure described in section 1105(c)(1) of this title),

(3) provide a procedure for amending such plan, and for identifying the persons who have authority to amend the plan, and

(4) specify the basis on which payments are made to and from the plan.

Section 414 of the Employee Retirement Income Security Act of 1974, 29 U.S.C. § 1114

§ 1114. Effective date

(a) Except as provided in subsections (b), (c), and (d) of this section, this part shall take effect on January 1, 1975.

(b)(1) The provisions of this part authorizing the Secretary to promulgate regulations shall take effect on September 2, 1974.

(2) Upon application of a plan, the Secretary may postpone until not later than January 1, 1976, the applicability of any provision of sections 1102, 1103 (other than 1103(c)), 1105 (other than 1105(a) and (d)), and 1110(a) of this title, as it applies to any plan in existence on September 2, 1974, if he determines such postponement is (A) necessary to amend the instrument establishing the plan under which the plan is maintained and (B) not adverse to the interest of participants and beneficiaries.

(3) This part shall take effect on September 2, 1974, with respect to a plan which terminates after June 30, 1974, and before January 1, 1975, and to which at the time of termination section 1321 of this title applies.

(c) Section 1106 and 1107(a) of this title (relating to prohibited transactions) shall not apply—

> **(1)** until June 30, 1984, to a loan of money or other extension of credit between a plan and a party in interest under a binding contract in effect on July 1, 1974 (or pursuant to renewals of such a contract), if such loan or other extension of credit remains at least as favorable to the plan as an arm's-length transaction with an unrelated party would be, and if the execution of the contract, the making of the loan, or the extension of credit was not, at the time of such execution, making, or extension, a prohibited transaction (within the meaning of section 503(b) of Title 26 or the corresponding provisions of prior law);
>
> **(2)** until June 30, 1984, to a lease or joint use of property involving the plan and a party in interest pursuant to a binding contract in effect on July 1, 1974 (or pursuant to renewals of such a contract), if such lease or joint use remains at least as favorable to the plan as an arm's-length transaction with an unrelated

party would be and if the execution of the contract was not, at the time of such execution, a prohibited transaction (within the meaning of section 503(b) of Title 26) or the corresponding provisions of prior law;

(3) until June 30, 1984, to the sale, exchange, or other disposition of property described in paragraph (2) between a plan and a party in interest if—

(A) in the case of a sale, exchange, or other disposition of the property by the plan to the party in interest, the plan receives an amount which is not less than the fair market value of the property at the time of such disposition; and

(B) in the case of the acquisition of the property by the plan, the plan pays an amount which is not in excess of the fair market value of the property at the time of such acquisition;

(4) until June 30, 1977, to the provision of services, to which paragraphs (1), (2), and (3) do not apply between a plan and a party in interest—

(A) under a binding contract in effect on July 1, 1974 (or pursuant to renewals of such contract), or

(B) if the party in interest ordinarily and customarily furnished such services on June 30, 1974, if such provision of services remains at least as favorable to the plan as an arm's-length transaction with an unrelated party would be and if such provision of services was not, at the time of such provision, a prohibited transaction (within the meaning of section 503(b) of Title 26) or the corresponding provisions of prior law; or

(5) the sale, exchange, or other disposition of property which is owned by a plan on June 30, 1974, and all times thereafter, to a party in interest, if such plan is required to dispose of such property in order to comply

with the provisions of section 1107(a) of this title (relating to the prohibition against holding excess employer securities and employer real property), and if the plan receives not less than adequate consideration.

(d) Any election, or failure to elect, by a disqualified person under section 2003(c)(1)(B) of this Act shall be treated for purposes of this part (but not for purposes of section 1144 of this title) as an act or omission occurring before the effective date of this part.

Section 502(a) of the
Employee Retirement Income Security Act of 1974,
29 U.S.C. § 1132(a)

§ 1132. Civil enforcement

(a) Persons empowered to bring a civil action

A civil action may be brought—

(1) by a participant or beneficiary—

(A) for the relief provided for in subsection (c) of this section, or

(B) to recover benefits due to him under the terms of his plan, to enforce his rights under the terms of the plan, or to clarify his rights to future benefits under the terms of the plan;

(2) by the Secretary, or by a participant, beneficiary or fiduciary for appropriate relief under section 1109 of this title;

(3) by a participant, beneficiary, or fiduciary (A) to enjoin any act or practice which violates any provision of this subchapter or the terms of the plan, or (B) to obtain other appropriate equitable relief (i) to redress such violations or (ii) to enforce any provisions of this subchapter or the terms of the plan;

(4) by the Secretary, or by a participant, or beneficiary for appropriate relief in the case of a violation of 1025(c) of this title;

(5) except as otherwise provided in subsection (b) of this section, by the Secretary (A) to enjoin any act or practice which violates any provision of this subchapter, or (B) to obtain other appropriate equitable relief (i) to redress such violation or (ii) to enforce any provision of this subchapter; or

(6) by the Secretary to collect any civil penalty under subsection (i) of this section.

Section 411(d)(6) of the Internal Revenue Code of 1954, 26 U.S.C. § 411(d)(6)

Prior to Amendment by Retirement Equity Act of 1984:

§ 411(d)

(6) Accrued benefit not to be decreased by amendment.— A plan shall be treated as not satisfying the requirements of this section if the accrued benefit of a participant is decreased by an amendment of the plan, other than an amendment described in section 412(c)(8).

Subsequent to Amendment by Retirement Equity Act of 1984:

§ 411(d)

(6) Accrued benefit not to be decreased by amendment.—

(A) In general.—A plan shall be treated as not satisfying the requirements of this section if the accrued benefit of a participant is decreased by an amendment of the plan, other than an amendment described in section 412(c)(8), or section 4281 of the Employee Retirement Income Security Act of 1974.

(B) Treatment of certain plan amendments.—For purposes of subparagraph (A), a plan amendment which has the effect of—

(i) eliminating or reducing an early retirement benefit or a retirement-type subsidy (as defined in regulations), or

(ii) eliminating an optional form of benefit,

with respect to benefits attributable to service before the amendment shall be treated as reducing accrued benefits. In the case of a retirement-type subsidy, the preceding sentence shall apply only with respect to a participant who satisfies (either before or after the amendment) the pre-amendment conditions for the subsidy. The Secretary may by regulations provide that this subparagraph shall not apply to a plan amendment described in clause (ii) (other than a plan amendment having an effect described in clause (i)).

Section 7805 of the Internal Revenue Code of 1954, 26 U.S.C. § 7805

§ 7805. Rules and regulations

(a) Authorization.—Except where such authority is expressly given by this title to any person other than an officer or employee of the Treasury Department, the Secretary or his delegate shall prescribe all needful rules and regulations for the enforcement of this title, including all rules and regulations as may be necessary by reason of any alteration of law in relation to internal revenue.

(b) Retroactivity of regulations or rulings.—The Secretary or his delegate may prescribe the extent, if any, to which any ruling or regulation, relating to the internal revenue laws, shall be applied without retroactive effect.

REGULATION INVOLVED

IRS Regulations
§ 1.401-1(b)(1)(i)

§ 1.401-1. Qualified pension, profit-sharing, and stock bonus plans—

(b) General rules. (1)(i) A pension plan within the meaning of section 401(a) is a plan established and maintained by an employer primarily to provide systematically for the payment of definitely determinable benefits to his employees over a period of years, usually for life, after retirement. Retirement benefits generally are measured by, and based on, such factors as years of service and compensation received by the employees. The determination of the amount of retirement benefits and the contributions to provide such benefits are not dependent upon profits. Benefits are not definitely determinable if funds arising from forfeitures on termination of service, or other reason, may be used to provide increased benefits for the remaining participants (see § 1.401-7, relating to the treatment of forfeitures under a qualified pension plan). A plan designed to provide benefits for employees or their beneficiaries to be paid upon retirement or over a period of years after retirement will, for the purposes of section 401(a), be considered a pension plan if the employer contributions under the plan can be determined actuarially on the basis of definitely determinable benefits, or, as in the case of money purchase pension plans, such contributions are fixed without being geared to profits. A pension plan may provide for the payment of a pension due to disability and may also provide for the payment of incidental death benefits through insurance or otherwise. However, a plan is not a pension plan if it provides for the payment of benefits not customarily included in a pension plan such as layoff benefits or benefits for sickness, accident, hospitalization, or medical expenses (except medical benefits described in section 401(h) as defined in paragraph (a) of § 1.401-14).